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Business Basics

Retail Buying Function

A Self-Instructional Booklet
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GUIDESHEET

BUYING FUNCTION/RETAIL STORES

INTRODUCTION

This booklet is part of a series intended to help small businesspeople increase their knowledge of, and skills in, various aspects of business management. Other booklets in the series may be obtained from the nearest Small Business Administration field office.

Buying Function/Retail Stores looks at techniques and practices that assure a business of a profitable and well organized buying plan. It covers the following topics:

- merchandise management
- the buying function, including the buying cycle
- forecasting needs
- open-to-buy
- selecting suppliers
- negotiating the purchase
- merchandise control

As a result of completing this booklet, the small businessperson should:

1. Be better able to better determine the needs of his or her business through effective forecasting and use of the open-to-buy formula.

2. Be more effective in selecting suppliers who offer quality goods at the right price.

3. Be more discerning when negotiating purchases for quantity, price, and terms of sale.

4. Be able to establish more effective methods for controlling merchandise.

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OUTLINE

BUYING FUNCTION - RETAIL STORES

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- Stock Records

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Sally Jones, the owner of a small gift shop, was wondering how she might best keep track of all her merchandise. "I can't possibly keep records of everything this store buys and sells. It would take so much time to record all the information, that I would have to work 100 hours a week to get everything done! So far, I've simply been using my judgement as to when to re-order and how much to buy. This doesn't seem to work very well though, since I often overbuy or have stockouts. Isn't there an easier way to keep track of merchandise?"

Bob Smith, the manager of a sporting goods store across town, was faced with a somewhat different problem. His present swim wear supplier offered to provide him with a quantity discount for large volume purchases. "Although I do sell a lot of swim wear, I'd have to buy more than a year's supply to get a good quantity discount. If styles don't change, it might be a real bargain. But on the other hand, if the styles do change, I'd really be sunk. I wonder whether I should chance the purchase?"

What Sally and Bob have in common is the need for a good BUYING PLAN for their respective retail businesses.

OVERVIEW AND PURPOSE

The purpose of this booklet is to help you gain greater knowledge and skill in the buying practices utilized in your store.

This booklet should help you to:

1. Gain a clearer view of the relationship between the buying and merchandise management functions.

2. Become more effective in applying the steps in the buying cycle, including:

   - planning the buying program
   - selecting suppliers
   - making the purchase
   - following up on the purchase

3. Develop better buying procedures for your store.

FORMAT

The information in this booklet is presented in a unique way. For example, following each key thought will be a question or series of questions to which you will be asked to respond. These questions will require you to restate the key points described in the paragraphs immediately preceding the question. In each case, you should write a few notes on how you would respond to the question directly on the page in the space provided so you will have it as a permanent record for review. NO NEED TO WRITE COMPLETE SENTENCES - just a few words to indicate your thoughts. A good answer to each question will be given in the box on the first even numbered page which follows the question. Your answers need not match the booklet answers exactly.

It will, of course, do you little good to look ahead at the answers before writing out your own. The whole purpose of this type of learning format is to give you a chance to see whether you clearly understand and remember the information by writing it out before you check the answer.

In addition to the questions, you will be asked to work on several on-the-job activities. These will be brief suggested assignments which will give you a chance to apply one or several of the concepts discussed in the booklet to actual work situations in your own firm. If possible, you should discuss these assignments with someone whom you consider knowledgeable in retail buying so you can benefit from any ideas which come up.

It is important to note here that this booklet is not intended to provide you with exhaustive information on this topic. Nor is it designed to tell you how to run your business. Rather, the booklet is intended only to increase your knowledge and skills by reviewing some basic practices that are appropriate for use in small firms. They can easily be modified to best serve the needs of your own firm.

INTRODUCTION

If you have ever taken a good look at the small retail stores in your community, you've no doubt noticed several which always seem to have just the right merchandise at just the right prices. It is obvious that such stores are run by capable managers with a good knowledge of their market! What is not obvious to the ordinary observer, however, is that these 'capable managers' are doing nothing more than following good buying techniques and merchandise management practices.

The Booklet Merchandise Management discusses the selection of merchandise based on its ability to bring a satisfactory profit - in terms of money invested and store spaces occupied.

This booklet, the Buying Function - Retail Stores, discusses the buying practices you need to secure the RIGHT merchandise, of the RIGHT quality, in the RIGHT quantity, at the RIGHT price, and at the RIGHT time.

It is strongly suggested that the Booklet, Merchandise Management be studied closely in conjunction with this booklet.

MERCHANDISE MANAGEMENT AND BUYING

Jointly, the functions of buying and merchandise management involves all the activities required to:

- find and select merchandise
- select and negotiate with vendors
- manage inventory
- decide on price and cut-price sales
- assign selling space to each merchandise line and item
- plan, design and implement advertising campaigns
- plan, design and implement in-store displays and promotion of merchandise

Most stores hardly distinguish between the functions of buying and merchandise management because the same person usually performs both. In large stores or chain stores, there are, however, different people in the buying and merchandise management position. While the respective responsibilities are not always the same in different firms, it is general practice for the buyers to select

and negotiate with vendors, and for merchandise managers to assign floor space to the various merchandise lines as well as decide on major promotions and advertising. Selection of merchandise, display of merchandise and other in-store promotion, pricing, inventory management, and decisions on sales are responsibilities which are shared in some firms and assigned to either function in others.

In many stores, buyers for several departments report to merchandise managers. Either the merchandise manager or the buyer, or both, are responsible for the profitability of the merchandise. In a small store, it is not very important as to who does what, whether the owner performs all the functions or whether others have some of these responsibilities. What is important, though, is that all these responsibilities are performed competently and thoroughly!

1. *What is the distinction between the buying and merchandise management function?*

   Your Answer: (Remember, in this question, as well as in future ones, there is no need to write complete sentences - just key words on how you are answering the question. A good answer is on page 6.)

THE BUYING FUNCTION

Goals of Good Buying

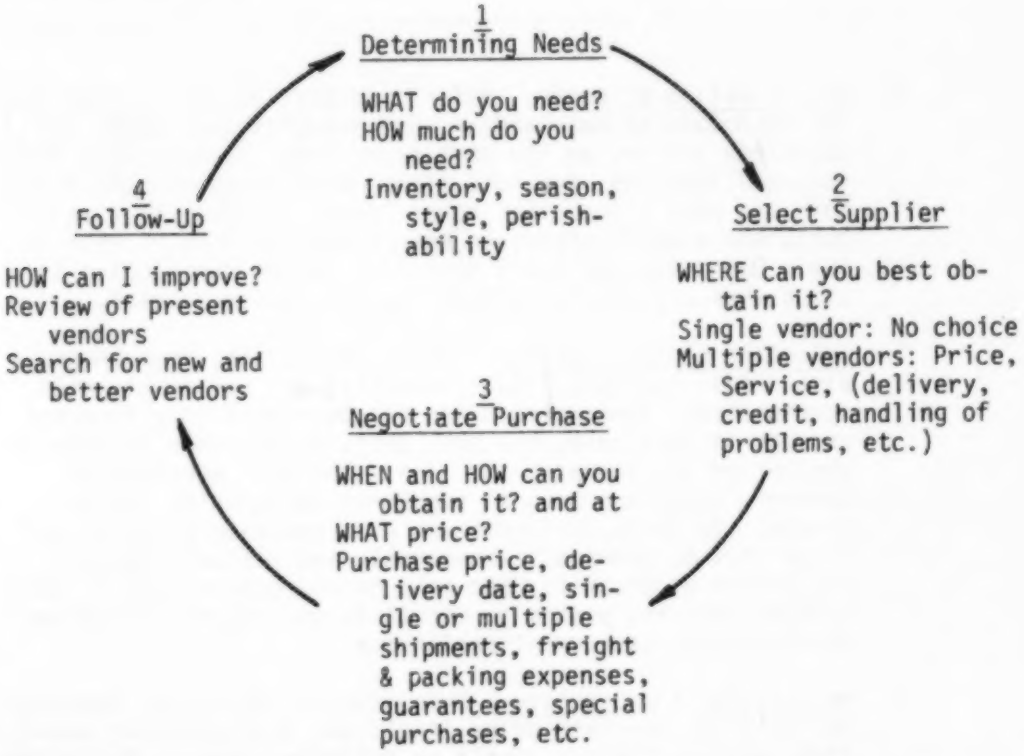
For people not acquainted with retailing, the work of a buyer may seem to be a relatively simple one - finding and purchasing the needed merchandise at a good price. As you know, there is a lot

more to buying than just bargaining with vendors. Not only are there other functions to consider, as just mentioned, but good buying involves buying the right merchandise for your customers:

- at the best price
- in the right quantity
- of the right quality
- from vendors who will be reliable and provide other valuable services

If all this is done thoroughly and competently, many considerations are involved. These are all described, in proper relationship, in the Buying Cycle.

The Buying Cycle


1
Determining Needs
WHAT do you need?
HOW much do you need?
Inventory, season, style, perishability
2
Select Supplier
WHERE can you best obtain it?
Single vendor: No choice
Multiple vendors: Price, Service, (delivery, credit, handling of problems, etc.)
3
Negotiate Purchase
WHEN and HOW can you obtain it? and at WHAT price?
Purchase price, delivery date, single or multiple shipments, freight & packing expenses, guarantees, special purchases, etc.
4
Follow-Up
HOW can I improve?
Review of present vendors
Search for new and better vendors

The process of buying involves four major steps. These steps apply regardless of the frequency in which you review your merchandise lines. They are:

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Book Answer

1. *There is no sharp line of distinction between buying and merchandise management; jointly, the two functions are responsible for the profitability of the merchandise selection.*

   When these two functions are not performed by the same person, the buyer usually selects and negotiates with vendors, while the merchandise manager assigns floor space to the various lines and decides on promotion and advertising.

   Selection of merchandise, management of inventory, pricing decisions, and in-store promotions including displays, are responsibilities which are sometimes shared and sometimes assigned to either function.

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1. Determination of needs. Before you buy, you must determine for each line of merchandise what you will need until the next time you review the particular line. Determining WHAT you need involves, for some items, merely looking at inventory and past sales. For other lines, it concerns risky decisions - WHICH styles to select and HOW MUCH of each to buy. One thing you don't want is a lot of merchandise in stock when a style is outmoded or the season is past.

2. Selection of the supplier. After determining your merchandise needs, you must find a vendor(s) who can supply this merchandise. Some merchandise can be bought only from one vendor; in this case, the only decision you have to make is whether or not to carry the line. For most merchandise, however, there are several suppliers among which you can choose. In these instances you must evaluate price as well as service in terms of: reasonable and reliable delivery; adjustment of problems; and help in emergencies and in other matters such as, possibly, credit terms, spaced deliveries, and inventory management assistance.

3. Negotiating the purchase. This crucial third step involves not only the purchase price itself but also concerns quantities, delivery dates, single or multiple shipment deliveries, freight and packing expenses, guarantees on the quality of the merchandise, promotion and advertising allowances, special offers on slightly damaged materials or sell-outs, etc.

4. Follow-up. Finally, to improve service, you must review your relationship with each vendor from time to time, to determine if changes should be made. As necessary, a search for alternate or new suppliers should take place.

2. *What are the goals of the buying function?*

Your Answer:

3. *What are the basic steps in the buying cycle?*

Your Answer:

Book Answer

2. *The buying function involves buying the right merchandise for your customers:*

   - *at the best price*
   - *in the right quantity*
   - *of the right quality*
   - *from vendors who will be reliable and provide other services*

Book Answer

3. *The buying cycle includes the following steps:*

   - *determining needs*
   - *selecting suppliers*
   - *negotiating the purchase*
   - *follow-up*

DETERMINING NEEDS

Different types of merchandise require different techniques to determine what is needed. It is therefore important to recognize, for the various merchandise lines in your store, whether they are primarily staples, seasonal items, or style or perishable items. Most businesses carry some merchandise in each of these categories. Effective management of the buying function means planning your buying program and your recordkeeping with the differences between these merchandise categories in mind.

The goal in each case, whether your merchandise be primarily staple, seasonal, style-oriented, or perishable, is to establish or maintain inventory at the lowest possible level and still have a sufficient variety of colors, sizes or models available from which customers can choose. Such a practice will minimize losses due to obsolescence and spoilage, while freeing capital which may be put to other worthwhile uses.

Forecasting Techniques

Staples

Staple or semi-staple merchandise is generally in demand year-round, with little change in model or style. Basic appliances, hardware, housewares, books, domestics, and basic clothing items like underwear and pajamas fall into this category. The staples in your store, even if yours is primarily a business of style or seasonal merchandise, not only bring you extra profit, but also serve as an incentive, bringing customers into the store who may then purchase some of your primary merchandise.

The important characteristics of staples is steady usage, enabling you to order more of them whenever needed. Deciding how much to buy, therefore, concerns primarily:

Sales trends - If you have records available which tell you how much of each staple you have sold during the past two or three months, and also how much of the same staple that you've sold during the same period in the previous year, you know whether the item has increased in popularity, or has remained the same. You can then decide, if the trend is up, whether you want to buy more and increase your average inventory, or whether you can again maintain the same sales trend without running out of stock.

Profitability - Items which bring you a better return on your investment in space and capital are the more desirable items to buy.

Discounts - These are usually available with quantity purchases. (Discounts will be discussed further, under 'Making the Purchase'.)

The combination of these factors will provide you with a general indicator of your needs in staple merchandise.

Seasonal Merchandise

Seasonal merchandise, as implied, is in demand only at certain times of the year. Obvious examples include sleds, snow tires, bathing suits, sun glasses, lawn equipment, and patio furniture. Although some seasonal items can be secured during peak demand to replenish your inventory, many are unavailable, or cannot be obtained quickly enough at this time. Therefore, such merchandise is best bought well in advance of the season.

Because seasonal items are fast moving in-season and slow moving or stagnant during the off-season, it is important to maintain your stock to satisfy this on-off movement. Determining your needs for seasonal items (predicting, forecasting) relies heavily on knowing what customer demand for that item or merchandise line was in the past. One method of knowing previous customer demand on seasonal items is by maintaining a month-by-month tally of unit(s) sold, either by dollar value or amount (numbers). These records then can be examined on a yearly basis enabling you to clearly see selling trends and make your buying decisions accordingly. One method of maintaining your records, is to use a separate sheet or index card for each merchandise item, group of items or entire line.* In the example below, note that in 1979, most of the sales on this item took place in April, and at the end of the season, 20 remaining items in inventory had to be sold below cost.

Merchandise Item: _____

Sales Record

	1979	1980	1981	1982	1983
January	-0-				
February	$50.				
March	$700.				
April	$2,200.				
May	$1,000.				
June	$300.				
July through December	-0-				
Total units bought	300				
Sold below cost	20				

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*Fortunately, the seasonal pattern can often be matched by merchandise line, and all items in that line can be treated similarly to simplify recordkeeping.

For the novice buyer who has no previous sales records to rely on, suppliers and their salespeople can serve as a good source of information for predictions.

Where orders cannot be placed during the season, or where suppliers could delay shipments, good forecasting is of utmost importance to help predict what quantity of each item will be needed for the season. Predictions can also include plans for a pre-season sale which would entice customers to buy from you rather than your competitors. The forecast can also consider any end-of-season sales you plan to run. If such late sales events are profitable, then it may not be difficult to decide what quantities are needed. If such sales are not profitable, then you have to estimate much more carefully so you won't be left with a large stock of slow moving or dead merchandise.

Unfortunately, there is no foolproof method of accurately predicting future sales. Usually, though, good prediction of future sales can be made from consideration of:

- your own past experience with the movement of the merchandise
- records of previous sales such as the one shown on page 10
- length of the season
- planned selling price
- planned advertising and promotion effort, including sales
- the extent to which there is an increase or decrease in competition
- predictions of consumer buying from trade journals

These factors together can give you a fairly good idea of the quantity of each item that you are likely to sell during the upcoming season.

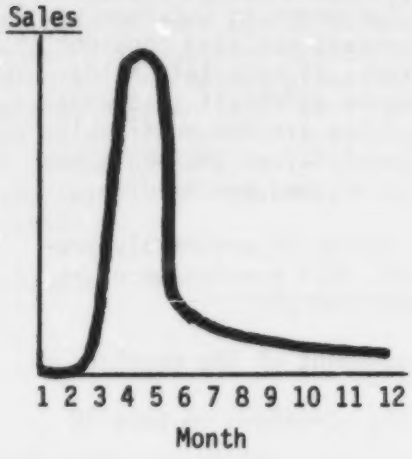
Style and Perishable Items

Items of style include such merchandise as fur coats, ladies' apparel, mens' apparel, sun glasses, and sportswear. Stylish items are usually more expensive than staples and seasonals. Because the demand for any particular style tends to increase rapidly, then drop off rapidly, overbuying in this area can have a disastrous effect on profits. Once a style is out, it is often very difficult to sell it at a profit.

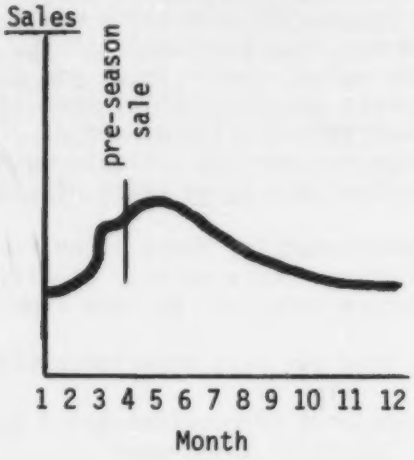
Perishable merchandise has similar characteristics. If you buy more than can be sold, some of it will begin to spoil and bring only a fraction of the normal price.

On those types of items where you have had sufficient difficulties in the past so that you feel they deserve detailed attention, you could plot the progress of different styles to see how they usually behave. A few examples of such graphs follow. They can help to predict how much to buy, and also when to buy.

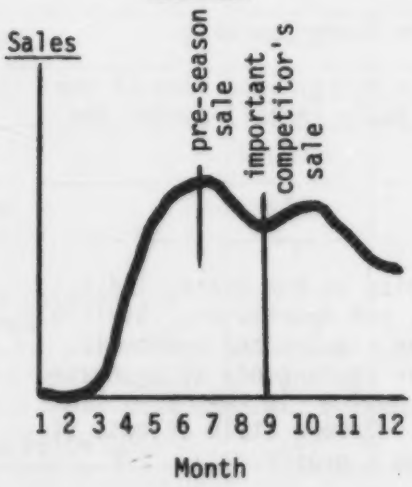
STYLE A



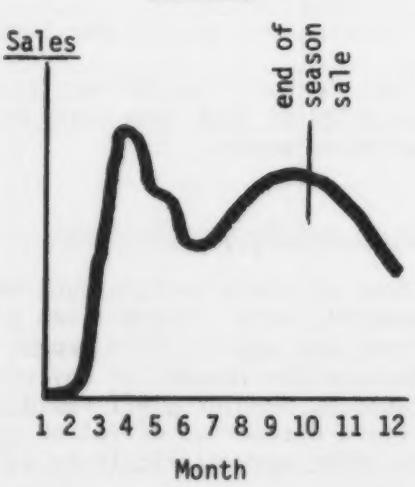
STYLE B



STYLE C



STYLE D



When plotting graphs, it is important to note all special, significant events such as your own sales and those of major competitors. These events also have to be planned or predicted, and kept in mind when forecasting merchandise needs.

Although graphs may not predict sales very accurately, they usually will narrow the amount of buying error made on items on which they are used. Sometimes, however, an overstock of non-seasonal goods occurs because of over-buying, or because the items are either unstylish or poor quality. In such a case, the amount of stock should be reduced as soon as possible to minimize the effect of any resulting loss.

4. *What are some factors that can help you predict the sales volume of seasonal merchandise?*

   Your Answer:

5. *How would you plot graphs of movement of style merchandise?*

   Your Answer:

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Book Answer

4. *Some factors which can help you predict the sales volume of seasonal merchandise include:*

   - *your own past experience with sales*
   - *records of previous sales*
   - *length of the season*
   - *planned selling price*
   - *planned advertising and promotion effort (including sales)*
   - *extent to which competition has changed*
   - *published predictions of consumer buying*

Book Answer

5. *Graphs of movement of style merchandise can best be plotted by:*

   - *laying out months on the horizontal axis*
   - *laying out unit sales or dollar sales on the vertical axis*
   - *highlighting all special events such as your own special sales or competitor's sales*

Open-to-Buy

The forecasting techniques discussed in the preceding paragraphs allow you to determine your general inventory requirements for the particular type(s) of merchandise to be sold. These general requirements then can be utilized to determine your actual inventory requirements, i.e., the quantity of an item that you are prepared to buy at a given time. This actual quantity of merchandise is referred to as 'open-to-buy' and is that amount of merchandise you will need to carry you through your buying period and the delivery period which follows. That is the time between the periodic dates you place orders for a particular item and the time period it takes the supplier to deliver the item. For example, if you review your stock once a month, your buying period is one month or 30 days. If your supplier takes one week to deliver the item to you, your delivery period is seven days.

With all types of merchandise, seasonal, style, and perishable items, Open-to-buy on a given item may be calculated using the simple formula below:

expected unit sales during the buying period
(+) expected unit sales during the delivery period (the time between order and delivery)
(-) units on order
(-) current inventory above safety stock*
(=) Open-to-buy

Example:

Assume the following situation:

You review stock once a month and expect to sell 30 units of an item during the coming month; i.e., an average of one unit per day.

Your supplier takes a week to deliver. It is now the end of the month and you have 10 units (above safety stock) left in inventory.

How many units should you buy if five units have still not been received from the last order?

Open-to-buy can be easily calculated with this information following the simple formula given above.

30 sales expected during the buying period (1 month)
(+) 7 sales expected during the one-week period for delivery
(-) 5 units on order
(-) 10 units currently in inventory (above safety stock)
(=) 22 units Open-to-buy

If you prefer to work with forms, the same answer can be obtained by following the simple step-by-step procedure outlined on page 16.

'Open-to-buy' thus provides a fairly specific indication of the quantity of merchandise you can practically buy. To determine the final quantity you will buy, your Open-to-buy figure should be adjusted according to each type of merchandise on the basis of discounts available, credit terms, item profitability, and other considerations which will be covered in the section Negotiating the Purchase.

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*Safety stock is the number of units you wish to always keep in stock to cover emergencies or delays in deliveries.

STEPS FOR DETERMINING OPEN-TO-BUY

1. Select the merchandise item or line for which you wish to determine open-to-buy..... an item
2. How many units do you expect to sell before the next time you review the merchandise?..... 30 units
3. How many units do you expect to sell during the delivery period (the time between placing an order and receiving delivery)?..... 7 units
4. How many units are already on order?..... 5 units
5. How many units are in current inventory above safety stock?..... 10 units
6. Open-to-buy (subtract lines 4 and 5 from lines 2 and 3)..... 22 units

6. What is Open-to-buy?

Your Answer:

7. What is your Open-to-buy if:

- *you expect to sell 30 units during the coming two weeks*
- *your inventory is already down to the 5 units you always want to have in stock*
- *6 units are already on order and the supplier needs 3 business days to deliver*
- *you plan to review the item in 2 weeks?*

Your Answer:

ON-THE-JOB ACTIVITY 1

Review several merchandise items or lines in your own store.

Based on past sales trends, try to determine your Open-to-buy for the merchandise. (You may use either the step-by-step procedure on page 16 or the simple formula on page 15.)

After determining your Open-to-buy, make adjustments where necessary, in the quantity you will order based on considerations of item profitability, type of merchandise, etc.

If possible, discuss your thoughts with a person whose opinion you respect; pursue any additional ideas which may result from such a discussion.

SELECTION OF SUPPLIERS

Of the suppliers you now have, some may be excellent, some acceptable, and some less than desirable. The first step toward replacing undesirable ones, or selecting suppliers for new merchandise you want to stock, is to obtain a list of those whom you could consider. Awareness of available suppliers and their services will place you in a position to choose the best one.

Sources of information concerning suppliers are plentiful. They include:

1. Salespeople - salespeople of your existing suppliers often provide excellent information concerning possible sources of supply. Many are well informed of alternative sources of non-competing lines and they can often suggest new services and new products. Since they call on many different businesses, salespeople are also a good source of information concerning merchandise selection of stores similar to your own located in different parts of their territories. All of this information is available to the alert, open-minded buyer who knows how to obtain it without devoting too much time to vendor representatives who call on them.

2. Trade Magazines - general and specialized trade journals often contain advertisements placed by suppliers, and articles which provide clues to desirable new sources.

Book Answer

6. Open-to-buy is the quantity you are prepared to buy at the time you are ready to place an order. It can be determined on the basis of the quantity you will need, in addition to your current stock, to carry you safely through the buying period plus one delivery period.

Book Answer

7. Using the simple formula on page 15, Open-to-buy is calculated as:

30 unit sales during the buying period (two weeks)
(+) 6 expected sales during the 3-day delivery period
(-) 6 units on order
(-) 0 units currently in inventory above safety stock
(=) 30 units Open-to-buy

3. Business Contacts - often your customers or other business contacts may be able to provide you with useful information concerning potential suppliers.

4. Trade Registers and Directories - Thomas' register of American Manufacturers is one of several widely used trade registers which contains information on the addresses, number of branches, affiliations and even financial standing of all leading manufacturers.

5. Trade Exhibits - provide an excellent opportunity for you to see a variety of new products and give you an opportunity to compare similar products of different manufacturers.

6. Yellow Pages - the yellow pages in your telephone directory contain listings of local suppliers.

Factors to be considered in determining the best supplier for your needs are:

- price and discounts
- quality
- reliability
- services
- accessibility

1. Price is the most important consideration in the selection of a supplier, provided that quality and service are equivalent to that of other vendors.

   Price has many dimensions since it includes quantity, discounts, special allowances, the chance to buy special lots, seconds, or sell-outs, and dating of invoices.

2. Quality, and assurance that quality is always the same, is almost as important as price and closely linked to it. Obviously, in selecting a supplier you want to be certain that you will rarely, if ever, receive a poor quality shipment.

3. Reliability of delivery from a supplier is important as unreliable delivery can create problems of stockout which result in sales loss. In addition, slow or unreliable delivery also requires the buyer to maintain larger average inventories which result in increased carrying costs.

   A good supplier will be reliable when you have a sudden emergency and need some quick supplies and will protect you when there are shortages of material due to a strike or disaster.

4. Services which suppliers might provide are many and include: spaced deliveries, allowing you to purchase a larger quantity than your store may immediately handle, thus giving you advantage of quantity discounts; recycling of packaging to reduce overall freight and packing expenses; providing advertising and promotional materials and displays to help promote merchandise; and give-aways, such as literature and bags for the customers.

   In some industries, suppliers will offer inventory services to retailers. Usually these are provided for a small fee but they can be quite valuable in helping the retailer manage inventory with greater efficiency.

5. Accessibility is another factor on which suppliers should be judged. It is often important to personally contact the supplier concerning special problems that may arise. A supplier difficult to contact is clearly not as desirable as one easy to reach.

Keeping these factors in mind can help you to:

- avoid mistakes in selecting suppliers
- compare vendors vying for your business
- provide a firm foundation for thorough negotiations

8. *What factors should be used in evaluating suppliers?*

Your Answer:

ON-THE-JOB ACTIVITY 2

Using the table below, review several of your vendors and develop plans for approaching them to remedy less desirable features of their relationship with you.

Vendor	Price and Discounts	Quality	Reli-ability	Services	Acces-sibility

If possible, discuss your thoughts with a person knowledgeable in this area; pursue any ideas which may arise from such discussion.

NEGOTIATING THE PURCHASE

Negotiating with suppliers involves:

- comparing quantity discounts with inventory costs
- negotiating quantities and price
- negotiating terms of sale
- negotiating special conditions
- negotiating miscellaneous related matters

Comparing Quantity Discounts with Inventory Costs

Frequently suppliers offer discounts for large volume purchases, enabling you to buy more than your Open-to-buy quantity. In this situation, you must consider:

- cash on hand
- merchandise movement
- present inventory
- cost involved in carrying the increased inventory
- credit plan availability
- split shipments of merchandise

If split shipments are offered, staple items pose no problem since you can ask for deliveries when you need them and still take advantage of the quantity discount. Similarly with seasonal items, if you can sell the entire quantity you are buying during one season you can buy more than you would normally buy if no discount were offered.

If split shipments cannot be obtained from the supplier, you must determine whether the discount will obliterate the extra carrying costs.

Carrying costs are high and include: interest on money invested, insurance, cost of space and sometimes spoilage or obsolescence. These can easily add up to and exceed 25% of the value of the average merchandise inventory per year.

When deciding whether a quantity discount is worthwhile, you must compare the money you save with the extra inventory carrying cost.

To determine the value of a quantity discount, use the following steps:

1. Determine the savings from the quantity discount.

2. Determine how much extra merchandise you would have to carry in inventory, and for how long. Note that you would not carry the entire amount of the extra purchases - only one-half that much, since you would be working off the extra stock. When the shipment first arrives you would indeed have the full amount of the extra merchandise in stock. But when it will be time to reorder, none would be left. Therefore, your extra stock is only the average - or one-half the extra merchandise you bought.

Book Answer

8. Suppliers can, and should, be evaluated on the basis of:

- *price and discounts*
- *quality*
- *reliability*
- *services*
- *accessibility*

3. Multiply the average extra stock by the carrying charge (which is usually 20% to 25%) to obtain the additional cost of carrying the extra stock for a year.

4. Determine the additional carrying costs for the period of time it will take to work off the extra stock.

5. Compare the savings from the quantity discount with the cost of carrying the extra inventory and decide whether it is worthwhile to buy the larger quantity.

For example, if you can save $500 by taking an extra $6000 of merchandise into stock, and if it will take you six months to work off the extra stock, the calculations would be as shown below:

cost savings (discount) = $500

extra inventory would be $6000 in the beginning and zero six months later, therefore. . .

average extra inventory = $3000

carrying costs of the average extra inventory = $3000 x 25% x ½ year
= $750 x ½ = $375

Actual savings = cost savings minus carrying costs = $500 - $375 = $125

Since the real savings from taking the discount would be only $125, this deal would be worthwhile only if you are quite certain that you can really work the extra inventory off in six months without getting stuck on any hard-to-sell merchandise.

9. *A supplier offers a special discount of 10% for purchases of $8000 or more. Assume that the retailer normally buys about $3000 of this merchandise and that it would take 3 months to work off the extra $5000 - if it is purchased. This is stable merchandise so the retailer considers the inventory carrying costs to be 20%. Calculate the savings and costs.*

   Your Answer:

ON-THE-JOB ACTIVITY 3

For one of the items in your line where the supplier offers a quantity discount schedule, calculate the best quantity to buy. Either assume that your inventory carrying costs are 20% or calculate what they actually are by adding the following:

- interest charges on the investment (money tied up in inventory)
- insurance costs on the inventory
- handling costs of moving the material onto the shelf or floor and keeping it arranged neatly, and
- shrink from spoilage, damage, or theft

If possible, discuss results with a person knowledgeable in this area; pursue any additional ideas which may come from such a discussion.

Negotiating Quantities and Price

There are several things you can do to place yourself in a favorable negotiating position. Some of them are:

1. Be prepared by having your figures ready on:

   - Open-to-buy
   - Best quantity from any previously available quantity discount schedule.

Book Answer

9. Savings are 10% of $8,000 or $800
Extra inventory = $5,000
Average extra inventory = $2,500
Cost of carrying the average extra inventory for one year = $2,500 x 20% = $500
Cost of carrying the average extra inventory for 3 months = $500 ÷ 4 = $125

This discount appears to be a good deal.

2. Know what the vendor's competitors offer.

3. Know as much as possible about the kind of agreements, if any, the vendor has made with other stores.

4. Conduct an effective interview by letting the vendor's representative sell you, even if you know her or him well and are fully prepared to buy. Always give the impression that you may have another vendor available.

Negotiating Terms of Sale

To run your business efficiently you must have reliable and prompt delivery. Furthermore, you want to keep the lowest inventory possible while keeping enough stock on hand to satisfy customer needs for an adequate selection. You also would like to sell as many units of a new shipment as possible, before you have to pay for it.

When negotiating a purchase, therefore, you want to obtain:

- prompt delivery
- split shipments
- as much time as possible after delivery to pay the bill (dating of invoices)
- cash discounts

Obviously, you cannot expect to get everything from your supplier all the time and still be considered a desirable customer. Therefore, you must use judgment on how aggressive you should be - especially since you may also like to negotiate special conditions on other matters.

Split shipments are important only when there are quantity discounts; if the vendor grants such split shipments to other customers, then there is no reason why you should not get them too.

The same is true of "dating" of invoices, a practice in which, at least at certain times of the year, some suppliers will permit you to buy and accept delivery but pay as much as 60 to 120 days after receipt of the merchandise.

The savings from dating can be significant, especially if your bank charges you 12% or more on your borrowings. Whenever you get 90 day dating on $1,000 of merchandise, your savings, at a 12% rate for bank money, amount to $30. Several such datings can bring a nice increase in net profits.

Though usually shown on vendor invoices, cash discounts at times have to be requested, These discounts often may be 1 or 2 percent or higher off the total order if you pay in full within 10 days.

Oftentimes the supplier may not tell you that split shipments or dating or cash discounts can be granted. It is up to you, therefore, to initiate bargaining for them.

Negotiating Special Conditions

Suppliers sometimes make available special allowances such as advertising or promotional allowances in proportion to purchase prices. Other factors that can reduce the cost of buying merchandise are special packaging or better shipping methods. Exploring all of these possibilities with suppliers can provide many small savings which, yearly, can be significant.

Negotiating Miscellaneous Related Matters

Still other ways for an astute buyer to increase profits exist in:

- seconds, leftovers, and sell-outs
- cooperative buying

Seconds, Leftovers, and Sell-outs

Very often it is possible to achieve much higher profit margins and run very effective promotions with manufacturer's "Seconds" or "Irregular" merchandise. Such merchandise is sometimes available with only minor damage at sharp discounts.

Similar to "Irregulars" are last season's leftovers, which are often desirable merchandise for customers who are not highly style conscious, as well as distress merchandise from manufacturers who are in financial trouble and need to liquidate their inventory quickly, possibly at cost or below.

The sharp buyer keeps a constant look out for opportunities to buy good quality merchandise of this type.

Cooperative Buying

Though used infrequently, cooperative buying does represent an excellent opportunity to reduce the cost of merchandise. If you can collaborate with another store in an adjoining community to purchase together those items where quantity discounts are available, significant savings may be possible.

10. *What are 5 steps you should keep in mind as you negotiate with suppliers?*

    Your Answer:

11. *What are some of the steps that can help you negotiate a better price?*

    Your Answer:

ON-THE-JOB ACTIVITY 4

Using the checklist on page 29, review your negotiating practices and plan your next negotiating session with an important vendor.

As in previous on-the-job activities, discuss your thoughts with a person knowledgeable in this area; pursue any additional ideas which may arise from such discussion.

Book Answer

10. The five steps to keep in mind when negotiating with suppliers are:

- *comparing quantity discounts with inventory costs*
- *negotiating quantities and price*
- *negotiating terms of sale*
- *negotiating special conditions*
- *negotiating miscellaneous related matters*

Book Answer

11. Some of the steps that can help you negotiate a better price are:

- *Be prepared by having your figures ready on:*
  - *o open-to-buy*
  - *o best quantity from any previously available quantity discount schedule*
- *Know what the vendor's competitors offer*
- *Know as much as possible about the kind of agreements, if any, the vendor has made with other stores*
- *Conduct an effective interview by letting the vendor's representative sell you, even if you know her or him well and are fully prepared to buy; always give the impression that you may have another vendor available*

SUMMARY/CHECKLIST FOR NEGOTIATING THE PURCHASE

Establish the best quantity to buy from a discount schedule if one exists

Negotiate quantity and price:

- be prepared; know your:
  - o open-to-buy
  - o best quantity from any previously available quantity discount schedule
- know what the vendor's competitors offer
- know what agreements the vendor offers to others

Conduct an effective interview with the vendor's representative

Negotiate terms of sale:
- delivery
- split shipments
- dating of invoices
- cash discount

Negotiate special conditions:
- advertising allowance
- promotion allowance
- packaging
- shipping method

Negotiate, or obtain information on:
- seconds or irregulars
- leftovers
- sell-outs

Consider cooperative buying

FOLLOW-UP

The last step in the buying cycle as discussed on pages 4 and 5 is follow-up.

Follow-up consists of continuous checking to find more desirable:

- suppliers
- merchandise
- buying and merchandise control practices

Finding better suppliers can be accomplished only be getting to know existing suppliers and being alert to information sources on new ones who may come into the market. Improving merchandise selection is a matter of Merchandise Management as discussed in Booklet 6. Better buying practices evolve from experimentation with improved methods whenever a problem appears.

Lastly, maintaining good merchandise control practices, as described below, will assure your success while operating within the buying cycle.

MERCHANDISE CONTROL

Good methods for controlling merchandise are invaluable in achieving the total benefits which can be derived from good buying techniques.

These control methods include stock rotation and record keeping.

Stock Rotation

Rotation of stock will assure that merchandise will not spoil while on the shelf. Two simple types of systems can help to achieve this:

- straight rotation or "two-bin" system
- color coding

Straight Rotation or "Two-bin" System

Straight stock rotation involves placing the last merchandise received physically behind or below the merchandise already in stock. The "two-bin" system applies primarily to small pieces of merchandise where storage in a box or bin facilitates handling. In this

variation, merchandise is kept in two bins or boxes which will be referred to as A and B. Box B contains enough merchandise to last through the delivery period, plus a "safety" stock. Box A contains enough to last through the buying period.

Merchandise is sold from bin "A" until it is empty, at which point an order is placed. While awaiting delivery, the merchandise in Box "B" is sold until the bin is empty. When the shipment arrives, bin "B" is refilled to cover the next delivery period safely. The remaining merchandise goes into bin "A".

In practice, two separate bins are not actually required. One bin large enough to hold the total quantity will be adequate if the "B" quantity can be kept separate in some way.

Color Coding

Color coding is another control technique that can assure good rotation. In this method, a record is kept of the date a shipment of merchandise was received and a color is assigned to the shipment. The price tag or label placed on the item will be of the assigned color. For example, the first shipment may have blue tags, the second one green tags, etc.

Alternatively, when a price is applied directly to the merchandise by a marking pen, the color marked is the same as that assigned the shipment.

Once the system has been in operation for more than one shipment, it is possible to tell at a glance which merchandise has been in stock the longest time. Besides helping with stock rotation, such color coding helps to reveal slow and fast moving items, thereby identifying merchandise for reduced price sales.

Stock Records

Stock records need to be kept only on merchandise where a physical, visual method of determining stock is fairly difficult.*

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*Since stock records in and of themselves do not rotate stock, one of the techniques discussed above will still have to be used to assure freshness of inventory.

One example of a stock record system that provides considerable information with relatively little effort is the Perpetual Unit Control Record shown on page 33. Such a record provides sales, cost, and inventory information for periods of two weeks to five months.

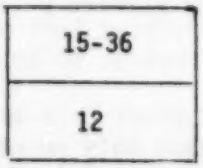
Information which is readily available from the Perpetual Unit Control Record is:

- items currently in stock
- sales trends over a five-month period
- high and low sales months
- comparative figures for the previous year
- wholesale costs and retail price
- delivery information: what has been ordered, what is in, and how long it takes to obtain a fresh supply
- minimum quantities
- ordering quantities

Not all this information needs to be recorded but you may find it all useful if you do. The form could easily be revised to suit individual needs, should records of additional information be needed.

Please note that the split boxes at the top of the record, i.e.:

refer to the two boxes on each item line:



For example, in the above, the size referred to is 15-36; the minimum quantity the retailer wants to keep in stock is 12 units.

12. *Describe techniques for maintaining good control over merchandise.*

Your Answer:

PERPETUAL UNIT CONTROL RECORD

Year - 1979

STYLE	size / min. qty.	min. pack / del. time	cost / retail	date	2-2	2-16	2-30	3-13	3-27	4-11	4-25	5-8	5-22	6-5	6-19	7-3	Quarterly sales
White Button Down Collar	15-36	6	28.50 dozen	on hand	24	23	22	22	20	19	20	17	17	15	16	16	this year: 8
				on order													
	12	1 week	3.95 ea.	rec'd													last year: 9
				sales*	1	1	0	2	1	-1	3	0	2	-1	0	0	
	15½-30	4	28.50 dozen	on hand	39	32	28	28	25	24	26	30	27	28	29	25	this year: 26
				on order						8							
	24	1 week	3.95 ea.	rec'd							8		2				last year: 31
				sales*	7	4	0	3	1	-2	4	3	1	-1	4	2	

*negative numbers indicate returns

Book Answer

12. Good control is maintained over merchandise when:

- *rotation techniques are used, either through straight rotation (the "two-bin" system) or some color coding system*

- *good records are maintained on all items where visual review is not convenient to establish the rate of sales and the inventory at any one time*

CONCLUSION

It is hoped, that techniques suggested in this booklet either will aid you directly or will motivate you toward searching for innovative techniques which will prove successful in the future.

Lastly, references to sources of information useful to the retailer are presented as guides to further your search for beneficial information - pursue, use and succeed.

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